IN THE

Supreme Court of the United States

October Term, A. D. 1923

No. 266

AIR-WAY ELECTRIC APPLIANCE CORPORATION,

Appellant,

vs.

HARRY S. DAY, TREASURER OF THE STATE OF OHIO, JOSEPH T. TRACY, AUDITOR OF THE STATE OF OHIO, JOHN R. CASSIDY, C. E. FORNEY, C. A. HORN, AS THE TAX COMMISSION OF THE STATE OF OHIO, AND THAD H. BROWN, SECRETARY OF THE STATE OF OHIO,

Appellees.

APPEAL FROM THE DISTRICT COURT OF THE UNITED STATES FOR THE SOUTHERN DISTRICT OF OHIO.

BRIEF FOR APPELLANT

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STATEMENT OF THE CASE

This cause comes to this court on appeal from an order sustaining the constitutionality of an Ohio statute imposing an annual franchise fee upon foreign corporations and denying a temporary injunction against its enforcement. Appellant, Air-Way Electric Appliance Corporation, is a corporation organized under the laws of Delaware, with an authorized capital stock of Four Hundred Thousand (400,000) shares without nominal or par value. (Record page 1 and 2). Fifty Thousand Four Hundred and Eighty-five (50,485) shares only were issued and outstanding at the time the fee in question was computed. (See Record page 35.)

At the time of its admission to do business within the State, in September of 1920, the value of the stock was fixed by the "Blue Sky" Commission of Ohio at Seven Dollars ($7.00) per share. (Record pages 2-3). All of its issued capital stock was sold at that price and the proceeds of approximately Three Hundred Fifty Thousand Dollars ($350,000) represents the corporation's total capital investment within the State.

A license fee of Four Thousand Fifty Dollars, ($4,050) was paid at the time of its entry into the State for the privilege of doing business in accordance with General Code Section 8728-1 and Sections 178, 179 and 180 (Record page 2).

Two specially constructed and equipped factory buildings were acquired in Toledo, Ohio, adapted to the manufacture and production of its products, consisting of electric sweepers, washers and sundry electric appliances, which said factories could not be disposed of except at a great loss. (Record, page 24-25.) From two to five hundred workmen and artisans were employed in these factories in manufacturing the articles above mentioned (Record page 25), which were sold to jobbers and dealers throughout the United States and foreign countries (Record page 23, 26 and 27). For this purpose a force of traveling salesmen was maintained who procured the orders from the customers at their places of business in the various states. The goods were then manufactured in the factories in Ohio and sent from them to customers or warehouses, some of which were located outside of the State, and payment was received by draft or check. (Record pages 2, 13, 23, 26, 27).

The appellant was at all times engaged in severe and very active competition with several domestic corporations in each and every line of its endeavors. (Record page 1, 43.)

The appellant is now and was at all times willing to pay to appellees any and all taxes which are justly found due and owing.

The following provisions of the General Code of

Ohio relating to the annual franchise fees payable by corporations, were in effect at the time of its admission and at the time the fee was computed:

> "Section 5499: *Foreign corporations Report.* —Annually, during the month of July, each foreign corporation for profit, doing business in this state, and owning or using a part or all of its capital or plant in this state, and subject to compliance with all other provisions of law, and in addition to all other statements required by law, shall make a report in writing to the commission in such form as the commission may prescribe."

Section 5501 provides the information required to be set forth in the report.

Section 5503 provides for the annual fee required of foreign corporations having stock *with* par value, and is as follows:

> *Collection: fee: minimum.*—On or before October fifteenth, the auditor of state shall charge for collection, as herein provided, annually from such company, in addition to the initial fees otherwise provided for by law, for the privilege of exercising its franchises in this state, a fee of three-twentieths of one per cent upon the proportion of the *authorized capital stock* of the corporation, represented by property owned and used and business transacted in this state.

which fee shall not be less than ten dollars in any case. Such fee shall be payable to the treasurer of State on or before the first day of the following December." (Italics ours.)

Section 5498 provides for the fee payable by domestic corporations having stock *with* par value, and is in part as follows:

"On the first Monday in August, the commission shall certify the amount so determined by it to the auditor of state, who shall charge for collection, on or before August fifteenth, as herein provided, from such corporation, a fee of three twentieths of one per cent. upon its *subscribed or issued and outstanding capital stock*, which fee shall not be less than ten dollars in any case." (Italics ours.)

Section 8728-11 as amended in February of ~~1919~~ 1920, 108 O. L., Part 2, 1287, provides for the fee payable by domestic and foreign corporations having stock *without* par value and is in part as follows:

"The amount of fees payable under section 5498" (domestic corporations) "by corporations formed or organized under this act shall be three-twentieths of one per cent. upon its subscribed or issued and outstanding preferred stock, plus *ten cents* for each share of common

stock, without par value, *subscribed or issued and outstanding*, but not less than ten dollars in any case.

"The amount of fees payable by a *foreign* corporation having stock without par value under section 5503" (foreign corporations) "shall be three-twentieths of one per cent. upon the proportion of the authorized preferred stock represented by property owned and used and business transacted in this state, and *one cent* for each share of *authorized common stock* without par value, but not less than ten dollars in any case." (Italics ours.)

Section 8728-11 was again amended by the act of May 17, 1921, 109 O. L. 273, to read as follows:

"The amount of fees payable under section 5498 by a corporation formed or reorganized so as to have common stock without par value shall be three-twentieths of one per cent. upon its subscribed or issued and outstanding preferred stock plus *five cents* for each share of common stock, without par value, *subscribed or issued and outstanding*, but not less than ten dollars in any case.

"The amount of fees payable by a *foreign* corporation having common stock without par value under section 5503 shall be three-twen-

tieths of one per cent. upon the proportion of the authorized preferred stock represented by property owned and used and business transacted in this state and *five cents* per share upon the proportion of the number of shares of *authorized common stock*, represented by property owned and used and business transacted in this state, but not less than ten dollars in any case." (Italics ours.)

In July of 1921 the report required by section 5499 was duly fi'ed by appellant, (Record page 3). This report showed property of the then value of Four Hundred Fifty-eight Thousand Two Hundred Seventy-eight Dollars ($458,278) owned by appellant, all of which was located within Ohio. (Record, Exhibit No. 2, following page 28.) Business was transacted during the preceding year in the amount of Two Hundred Fifty Thousand Five Hundred Ninety-four Do'lars ($250,594) all of which was stated to have been handled from Ohio. (Record, Exhibit No. 2, following page 28.) Upon the basis of this report a tax bill was rendered by the Treasurer of State to appellant for Twenty Thousand Dollars ($20,000), which upon its face is stated to have been computed in accordance with section 5503 of the Genera! Code, but which was obviously computed under section 8728-11 as amended by the act of May 17, 1921. (Record Exhibit No. 1 following page 28.)

In figuring the fee the entire property and business of the corporation was considered as being owned and having been transacted within the State. The tax was in fact computed at five cents per share on the entire 400,000 shares of *authorized* stock.

A protest against the amount and validity of the tax was made by letter and personal interview to the Tax Commission in which it was stated that a large portion of the business transacted was outside of Ohio. (Record page 28-29.) The Commission refused to grant a reduction of the tax or an opportunity to amend the report to show the business alleged to have been transacted outside of the State. (Record page 29.)

On December 9, 1921, the present suit was instituted in the District Court for the Southern District of Ohio, Eastern Division, in which a temporary injunction against the collection of the tax was sought upon the grounds, among others that section 8728-11 and section 5503 of the General Code were in contravention of the due process and equal protection clause and commerce clause of the Federal Constitution and in violation of Section 2, Article 12, and Section 29, Article 2, and Section 28, Article 2, and Article 1 of the Constitution of the State of Ohio and Article 1 of The Bill of Rights to the Ohio Constitution.

Upon a hearing before Judges Donahue C. J., Sater and Peck, D. Js., reported 279 Fed. 878, it was decided

that none of the constitutional objections urged were valid; but the bill was retained pending an application for rehearing to the Tax Commission in order that any errors as to the amount of business transacted within the State could be corrected and the tax assessed on the basis of the amended return. Thereafter such an application was filed, reciting that the business transacted in Ohio should have been stated to be Seventy Thousand Eight Hundred Two and 30-100 Dollars ($70,802.30) instead of Two Hundred Fifty Thousand Five Hundred Ninety-four and 58-100 Dollars ($250,594.58), as set forth in the original report and that the business transacted outside of Ohio should have been stated to be One Hundred Seventy-nine Thousand Seven Hundred Ninety-two and 28-100 Dollars ($179,792.28) making the aggregate of the property owned, and business transacted, in Ohio Five Hundred Twenty-eight Thousand Eight Hundred Eighty and 86-100 Dollars ($528,880.86) in place of Seven Hundred Eight Thousand Five Hundred Eighteen and 56-100 Dollars ($708,518.56). (Record page 19.)

The application was denied by the Tax Commission upon the ground that it had no jurisdiction to entertain an application more than sixty (60) days after the certification of the amount of the tax to the Auditor of State. (Record page 17.)

An amendment and supplement to the bill of complaint was filed April 6, 1922 setting forth the fact of the

application and its denial by the Tax Commission. (Record page 16.) Upon consideration a majority of the Court found that the correction sought should have been allowed, and that a tax based on the entire business transacted would be an unconstitutional interference with interstate commerce. The Tax Commission and other state officials were enjoined from collecting or attempting to collect a tax greater than Fourteen Thousand Nine Hundred Twenty-six Dollars ($14,926) which is the amount of the tax as computed on the basis of the amended report in accordance with the rule provided by Section 8728-11 as amended by the act of May 17, 1921. (Record page 54.)

Air-Way Electric Appliance Corporation appeals from the portion of the decree denying the full relief prayed for by it, upon the ground that the law under which the fee was assessed is unconstitutional. A cross appeal has also been taken by the State from the portion of the decree enjoining the collection of the tax in excess of that computed on the basis of the amended report. The grounds for appellant's appeal only will be discussed in this brief.

ASSIGNMENT OF ERRORS

The plaintiff prays an appeal from the interlocutory order of the Court below, made and entered herein on the 24th day of February, 1923, to the Supreme Court of the United States and assigns for error:

First. Said court erred in finding that Sec. 8728-11 of the General Code of Ohio is not in contravention of the Constitution of the United States, especially of the equal protection and due process clauses of Sec. 1, Art. XIV.

Second. The said court erred in finding that Secs. 5503 and 8728-11 of the General Code of Ohio are not in contravention of the Constitution of the United States, especially of the equal protection clause of Sec. 1, Art. XIV, and the privilege and immunity clause of Sec. 2, Art. IV.

Third. Said court erred in finding that Secs. 5503 and 8728-11 of the General Code of Ohio are not in contravention of the Constitution of the United States, especially of the interstate commerce clause of Sec. 8, Art. I.

Fourth. The said court erred in finding that Sec. 8728-11 of the General Code of Ohio is not in contravention of the Constitution of Ohio especially of the retroactive clause of Sec. 28, Art. II and Art. I of the Bill of Rights.

Fifth. The said court erred in finding that Secs. 5503 and 8728-11 of the General Code of Ohio are not in contravention of the Constitution of Ohio, especially of the uniform rule clause of Sec. 2 Art. XII.

Sixth. The said court erred in determining the tax at the rate of five cents (5c) per share on the proportion of the authorized capital stock without par value, represented by property owned and business transacted within this state without regard to its true value or its value as determined by the Securities Commission of Ohio.

Seventh. The said court erred in not granting a temporary injunction against the collection of any part of the tax as assessed.

PROVISIONS OF THE CONSTITUTION OF THE UNITED STATES AND OF THE STATE OF OHIO INVOLVED

First. Section 1, Fourteenth Amendment to the Constitution of the United States:

> "nor shall any state deprive any person of life, liberty or property without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws."

Second. Section 8, Article 1 of the Constitution of the United States:

> "Congress shall have power******to regulate commerce******among the several states."

Third. Section 2, Article 1 of the Bill of Rights of the State of Ohio:

> "All political power is inherent in the people

Government is instituted for their equal protection and benefit******."

Fourth. Section 2, Article 12 of the Constitution of the State of Ohio:

"Laws shall be passed taxing by uniform rule all moneys, credits, investments in bonds, stocks, joint stock companies or otherwise and also all real and personal property according to its true value in money******."

Fifth. Section 19, Article 1 of the Bill of Rights of the Constitution of the State of Ohio:

"Private property shall ever be held inviolate but subservient to the public welfare******."

Sixth. Section 28, Article 2 of the Constitution of the State of Ohio:

"The general assembly shall have no power to pass retroactive laws, ******".

ARGUMENT

1.

The Basis Taken for the Computation of the Annual License Fee Bears No Relation to the Value of the Privilege Conferred

The court will observe we are not concerned with the initial or admission fee charged against foreign corporations for the privilege of coming into the state, but

rather with the secondary fee charged for the annual privilege of carrying on business within the state. However drastic the power of a state may be concerning the former, in respect to the latter it is well settled that the fee which may be charged a foreign corporation is limited by certain provisions of the Constitution of the United States, to-wit: Interstate commerce, due process of law, and equal protection of the laws clauses; likewise there are certain provisions of the Constitution of Ohio and the Bill of Rights beyond which such a law cannot go, to-wit: Private property shall ever remain inviolate but subservient to the public welfare—the equal protection clause and the common welfare provision *supra*.

The Supreme Court of Ohio in the case of *Southern Gum Co. v Laylin*, 66 O. S. 578, had under consideration a portion of our present corporation tax law as applied to domestic corporations having stock of a designated par value, whereby a fee was charged upon the number of subscribed, issued and outstanding shares of stock. The Court, speaking through Burkett, J., said:

> "While there is no express limitation upon the power of the general assembly to tax privileges and franchises, such power is impliedly limited by those provisions of the constitution which provide that private property shall ever be held inviolate, but subservient to the public welfare, that government is instituted for the equal protection and benefit of the

people, and that the constitution is established to promote our common welfare.

"By reason of these limitations a tax on privileges and franchises can not exceed the reasonable value of the privilege or franchise originally conferred, or its continued annual value thereafter. The determination of such values rests largely in the general assembly, but finaliy in the courts."—(Syl.)

The privilege which appellant corporation has enjoyed for one year in Ohio was to use and own property of the value of $458,278 upon which it must pay the usual property taxes, and to do business in the state to the extent of $70 802.30. (Record pages 16 and 17.) The lower court fixed the fee chargeable for the year 1921 at $14 926.00. Such a fee, when considering the privileges conferred is far above the continuing value thereof and is unreasonable and in fact confiscatory.

The basis upon which the tax is computed bears no relation to the value of the privilege conferred. First, it takes the proportion of the number of shares of *authorized* stock represented by property owned and used and business done within the state, and, second, it multiplies that number by an arbitrary figure of five cents.

An initial fee based upon the authorized stock is usual, both when a new domestic corporation is formed and when a foreign corporation becomes domesticated.

Beyond that any fee for the privilege of carrying on business based upon *authorized* stock, unless it is reasonably limited in its maximum amount, is an anomaly, and unjustifiable.

Until appellant has sold all of its stock, to-wit: 349,515 shares more at $7.00 per share, the annual privilege which it enjoys to do business in this state is as a matter of fact, necessarily limited by the amount of its *issued* stock. If more stock is issued during any year it would be so reported the next year. The annual charge is computed not upon the *issued* stock but upon the *authorized* stock including both issued and unissued upon the number of shares of its authorized stock represented by property owned and business transacted for the preceding twelve months and is a charge in advance for the following year. Unissued stock, however, represents nothing and can have no relation to property owned or business transacted. Hence a fee computed on such a basis is unreasonable and unjust.

Various methods of computation have been used by different states. New York, for example takes the proportion which the corporation's actual capital employed within the state bears to its entire capital. Other states take the proportion of the subscribed or issued capital stock represented by property owned within the state: while another method used is to measure the fee by the business transacted within the state. It will be noticed

that in each of these methods the basis taken is indicative of the value of the privilege conferred. This is accomplished directly under a plan where the actual capital employed within the state is taken, and indirectly where the *issued* stock represented by the capital employed within the state is used.

When a basis of taxation is taken which does not reflect the value of the privilege sought to be taxed, there is a want of due process of law and a denial of the equal protection of the law. This is well illustrated by the situation presented in *Looney vs. Crane Co.*, 245 U. S. 178, and *International Paper Co. vs. Massachusetts*, 246 U. S. 135. 142 in which it is held that an annual franchise tax upon a foreign corporation measured by all of its property and business is unconstitutional, for the reason that the value of the exercise of a corporate franchise within the state is not indicated by its entire business and property transacted and owned.

The charge of five cents a share upon each share of *authorized* stock is also arbitrary and unjust as there is no logical connection between that charge and the value of that proportion of the privilege represented by that share If the legislature can fix an arbitrary fee of five cents per share without any justification therefor, what is to keep them from making the charge five dollars per share?

The fee originally imposed by Section 5503 of the General Code upon foreign corporations having stock

with par value is three-twentieths of one per cent upon the proportion of the authorized capital stock represented by property owned and used and business transacted within the state. This cannot be applied in case of corporations having stock *without* par value, and to cover this situation Section 8728-11 of the General Code, as amended 109 O. L. page 273, provides that in the case of corporations having stock without par value the fee shall be computed at the rate of five cents per share upon the proportion of the *number of shares* of *authorized* common stock represented by property owned and used and business transacted within the state. The Ohio Statute thus takes the designated proportion of the *number* of shares which the corporation *is authorized* to issue as the basis for computing the fee at five cents per share, although the shares may represent anything from one cent to one hundred dollars or more of actual investment or property instead of using some basis of computation having *some* relation to the value of the assets or the business transacted within the state.

A corporation's capital stock can be properly used as a medium for determining a tax based on its business transacted and property used within the state, only when it fairly reflects the value of the franchise granted. The par value of the issued stock does this to a certain extent, since money or property has been received by the corporation for the stock, but the number of shares into which the authorized issued and unissued stock is divid-

ed has no relation whatever to the value of the property of the corporation or the business transacted by it.

A "share of stock" is a unit of measure of variable size and value which is used to designate units of a corporation's capital stock. To attempt to determine the value of the business transacted and property owned by a corporation, and consequently the value of its franchise, by the number of variable units into which the stock is divided, is analogous to the determination of the value of farms by the number of fields into which they are divided or the value of fluids by the number of cans in which they are contained. Certainly the number of fields or cans could not be considered a reasonable basis for determining the value of the farms or fluid. The unsoundness of such a basis is clearly pointed out in the well reasoned cases of *Farrington vs. Mensching*, 187 N. Y. 8, and *People vs. Walsh*, 195 N. Y. S. 184, commented upon elsewhere in this brief.

We submit that any law which attempts to tax a privilege without limit must be charged upon a real rather than on an assumed basis, and not by multiplying unissued stock which represents nothing by a wholly arbitrary figure the result of which does not and cannot reflect the true value of the privilege, otherwise such a law confiscates property without due process of law in contravention of both the Constitution of the United States and of Ohio.

2.

There is an Arbitrary Discrimination Between Domesticated Foreign Corporations Having Par Value Stock and Those Having Non-Par Value Stock, Amounting to a Denial of the Equal Protection of the Law.

Under Section 5503 of the General Code of Ohio, the fee chargeable against foreign corporations having par value stock is three-twentieths of one per cent on the proportion of its authorized capital stock, which, in dollars and cents, amounts to fifteen cents on each one hundred dollars par value. Concerning the first issuance of such stock, it is fair to assume that such a corporation received property in payment for that stock in an amount equal to the par value thereof, or cash in an amount of at least eighty-five per cent thereof as fifteen per cent is the maximum amount allowed as a commission to underwriters under the Blue Sky Law, Section 6373-12, General Code of the State of Ohio. A corporation having stock without par value may issue and sell its shares for such consideration as shall be the fair value of such shares as fixed by its board of directors, or for such consideration as shall be consented to in writing by all the stockholders, or as fixed by a majority of the stockholders at a meeting called for the purpose. Gen. Code of Ohio, Sec. 8728-1. Since the Commissioner of Securities allowed appellant corporation to sell its stock at seven dollars ($7.00) per share, the State of Ohio then

set the maximum price at a figure which, in the opinion of its officers, was a fair value therefor. We submit there is a denial of the equal protection of the law under the Fourteenth Amendment of the Constitution of the United States and the provision of the Preamble of the Constitution of the State of Ohio, when the law provides for a fee against one domesticated foreign corporation of three-twentieths of one per cent (3/20%) and against another corporation of the same class a fee which, in the instant case, amounts to one and four-tenths per cent (1.4%), or a charge nearly ten times as great. Such is an assumed rather than a substantial basis for a privilege fee. The authorities supporting the above contention are discussed under the next heading.

3.
There is an Arbitrary Discrimination Between Various Domesticated Foreign Corporations Having Non-Par Value Stock Amounting to a Denial of the Equal Protection of the Law.

A second arbitrary discrimination between domesticated foreign corporations for the fee imposed is that it does not bear with substantial equality upon all of such corporations having non par value stock.

The fee imposed by Section 8728-11 of the General Code, in attempting to measure the value of the corporation's assets by the number of shares which it is authorized to issue, in effect subclassifies the foreign corpora-

tions subject to the fee upon a basis which bears no relation whatever, whether reasonable or unreasonable, to the franchise granted. The corporation may, of course, never issue its remaining authorized stock and until issued it cannot be considered as a reasonable basis for classification.

That the legislative power to classify for the purpose of taxation is limited by the requirement that the basis of the classification must bear a reasonable relation to the purposes for which the classification is made, has been repeatedly held by this Court. The principle is clearly stated in the following excerpt from the opinion in *Southern Railway Company v. Greene*, 216 U. S. 400, 417.

> "While reasonable classification is permitted, without doing violence to the equal protection of the laws, such classification must be based upon some real and substantial distinction bearing a reasonable and just relation to the things in respect to which such classification is imposed; and classification cannot be arbitrarily made without any substantial basis. Arbitrary selection, it has been said, cannot be justified by calling it classification."

Among other authorities laying down this principle are *Atlantic Coast Line Company v. Doughton*, 67 Lawyers Coop. Ad. Op. 681, 683; *Raymond v. Chicago Traction Company*, 207 U. S. 20, 38; *Greene v. Louisville & Interurban Railroad Co.*, 244 U. S. 499, 514;

Gulf, Colorado & Santa Fe Ry. v. Ellis, 165 U. S. 150, at 151, 155, 159 and 160; *Connolly v. Union Sewer Pipe Co.*, 184 U. S. 540 at 560, 561; *Cotting v. Kansas City Stock Yards*, 183 U. S. 79 at 111 and 112; *Magoun v. Illinois Trust & Savings Bank*, 170 U. S. 283 at 294; *Michigan Central R. R. v Powers*, 201 U. S. 245 at 293; *Hayes v. Missouri*, 120 U. S. 68, at 71 and 72; *Kentucky R. R. Tax Cases*, 115 U. S. 321 at 337; *Barbier v. Connolly*, 113 U. S. 27 at 32; *Commonwealth v. Sharon Coal Company*, 164 Pa. 304; *Commonwealth v. Shamokin*, 3 *Dauphin Co. Rep.* 168; *Commonwealth v. L. S. & M. S. R. R.*, same p. 172; *Commonwealth v. Jamestown R. R.*, same p. 214; *Commonwealth v. Coal Co.*, same p. 220., 60 L. R. A. p. 372; *State v. Township*, 36 N. J. L. 66; *In Re Jacobs*, 98 N. Y. 98; *People v. Marx*, 99 N. Y. 377.

It is also well settled that when a state law establishes a class and lays down a rule for taxing its members, the application of the rule must be such as will result in substantial equality as between the members of the class. The principle is well stated in *Gas Realty Company v. Schneider Granite Company*, 240 U. S. 55, 58, where in considering an assessment ordinance it said:

> "But as is implied by *Houck v. Little River Drainage District*, if the law is of such a character that there is no reasonable presumption that substantial justice generally will be done, but the probability is that the parties will be taxed disproportionately to each other and to the benefit conferred, the law

cannot stand against the complaint of one so taxed in fact. *Martin v. District of Columbia*, 205 U. S. 135, 139."

The principle for which we contend and the reasoning upon which it is based is well stated in the leading case of *Farrington v. Mensching*, 187 N. Y. 8, 79 N. E. 884, in which a law imposing a stamp tax upon transfers of stock was under consideration. Chapter 414, P. 1008 of the Laws of New York, 1906, provided for a tax on all transfers of stock of two cents "on each share of One Hundred Dollars of face value or a fraction thereof." The effect of this provision was to levy a two-cent transfer tax upon each share of stock as such, no matter what its par or actual value might be. The statute was declared unconstitutional for the reason that it resulted in an arbitrary and discriminatory classification in contravention of the equal protection clause of the Fourteenth Amendment. The Court, speaking by Vann J., in pointing out that classification for purposes of taxation must have some basis other than chance or accident, said:

> "The act now before us does not classify by arranging according to quality, but by arranging according to accident. *While it places all corporate shares in a class still it does not treat all members of the class alike but without method or order bears heavily upon some and lightly upon others, which, in effect, is a further classification.* Thus it imposes

the same tax on the sale of dollar shares and hundred dollar shares. *The tax is measured by the number of shares regardless of face value or actual value.* Shares of the same corporation might be taxed ten times as much or only one-tenth as much in one year as compared with the next, if simply the face value of each share were changed without changing the aggregate of the face value of all the shares, or the amount of capital invested, or the value of the assets in which it was invested. Shares are so classified as to tax the sale of those issued by one corporation several times as much as those issued by another of the same kind and in exactly the same situation without any reason for the distinction. *Possibly a valid distinction might be founded on the nature or object of the corporation or on the fact that it enjoyed special privileges,* putting banking and railroad corporations in and leaving manufacturing corporations out, for instance, *but we think none can rest on an accidental and non-essential quality without the violation of fundamental principles.* While the legislature has wide latitude in classification its power in that regard is not without limitation, for the classification must have some basis, reasonable or unreasonable, other than mere accident, whim or caprice. There must be some support of taste, policy, difference of situation or the like, some reason for it even if it is a poor one." (Italics ours).

"The serious objection to the statute under consideration is not that in some abnormal instance of low face value the tax might amount to confiscation, but that the classification is as purely arbitrary as the division of land into fields to which we have alluded. Granting the almost unlimited power of the legislature to classify as it sees fit, still there is no plausible or possible reason why one hundred acres in a single field should not pay the same tax as one hundred acres of equal value in ten fields. It seems equally clear that no distinction in liability to taxation can be drawn between ten shares of the face value of one hundred dollars each and one hundred shares of the face value of ten dollars each. If the corporations have equal assets and are equally successful, the two lots of shares are exactly the same thing. Suppose the entire capital is one hundred thousand dollars, ten shares of one hundred dollars each, or one hundred shares of ten dollars each would represent the same proportion of the corporate property. In other words, the fraction representing the equitable ownership would be exactly the same in each case."******

"The owners of corporate stocks do not stand on an equal footing under the statute. They do not receive the equal protection thereof, for some have to pay more than others in the same situation. Thus, if A. sells one hundred shares of the face value of $10.00 each for $1 000 he is taxed $2.00, while B.,

who sells ten shares of the face value of $100.00 each for $1,000 is taxed twenty cents, the thing sold in each case being worth the same amount. This is not classification but arbitrary or accidental selection."

Following the doctrine of the *Mensching* case, a franchise tax upon corporations having stock without par value was held to contravene the equal protection clause in *People v. Walsh*, 195 N. Y. Sup. 184, (Sup. C. App. Div. 3rd Dep.). Section 214, Chapter 640 of the Laws of New York 1920, provided that for the purpose of determining the annual franchise tax to be paid by foreign corporations having stock without par value, the no par value stock should be deemed to have a value of $100.00. The validity of arbitrarily providing for a value having no relation to the value of the privilege sought to be taxed, was attacked. The case was argued before Judges Cochrane, P. J., and Kellogg, Kiley, Van Kirk and Hindman, JJs. In a carefully considered opinion the Court, speaking by Kellogg J., in sustaining the contention that the tax contravened the equal protection clause of the Federal Constitution, said, (after quoting from the opinion of Judge Vann, in *Farrington v. Mensching* supra):

"* * * The compulsory valuation of $100.00 required by the provision as thus construed to be placed upon every share of no par value stock is entirely arbitrary, and necessarily will result in unequal taxation. It will require corporations having issued

stock of the value of $5.00 per share to pay the same tax per share as corporations having issued stock, the shares of which were in fact worth $100,000 per share. It might have the result of compelling corporations employing in this State a capital of only $1,000 for the privilege of doing their limited business, the same tax as corporations employing within the State a capital of $200,000."

This case was quoted from with approval in *Staples v. Kirby Petroleum Company*, 250 S. W. 293 (Court of Civil Appeals of Texas), in which the same taxing provision in regard to corporations having stock without par value was under consideration.

We submit that the same arbitrary classification denounced in the *Mensching* and *Walsh* cases supra, necessarily results from the application of the Ohio statute under consideration, and that the reason for which the New York statutes were declared unconstitutional also exists in regard to the Ohio law. True, as the lower court pointed out, the New York law measures the franchise fee required of a foreign corporation by the actual capital used within the State, whereas the Ohio law takes the authorized capital stock as the basis for the tax. Since, however, the objection to the law is that the basis for determining the tax has no relation to the value of the privilege it is not apparent how the inequality will be lessened by taking authorized instead of used capital as the basis. A second distinction, that the Ohio law bases the fee at

a fixed amount per share, whereas the New York law is fixed at a certain per cent and gives the stock a fictitious value, is also immaterial in its effect. By placing an arbitrary value upon the stock, the result is to require a different tax upon corporations having capital of the same value. By measuring the tax at a fixed amount per share, the same result follows. This is made clear by a comparison of the appellant's situation under the New York and the Ohio laws. The actual value of appellant's stock without par value, as fixed by the Commissioner of Securities in 1920, was $7.00 per share, making the actual capital invested approximately $350,000. The value of shares of other corporations having the same actual investment may be fixed at one thousand dollars per share and the number of shares correspondingly reduced with the result that the fee paid will only be a small fraction of that required of appellant. Under the New York law the value of appellant's stock would be fixed at $100.00 per share in the same manner as stock worth $1 000, and the same inequality would result.

The actual determination of the value of the stock by the State Securities Commission in effect fixes the par value of the stock, that is the price at which it must be sold, and it therefore represents the money or property with which the corporation began to do business in the same manner as stock having par value. This is easily ascertained and can be conveniently applied. The argument of necessity, therefore, if it ever could justify an arbitrary classification, does not exist in this case.

4.

A Law is Unconstitutional Which Taxes a Franchise on the Basis of a Corporation's Authorized Non Par Value Stock at an Arbitrary Value Far in Excess of the Value Fixed for Its Sale by the State.

When one department of a state has fixed the value of non par stock at a set price, any law which taxes the privilege of doing business within its confines computed on its stock on a basis far in excess of the value theretofore fixed, amounts to the taking of property without due process of law. Such an overlooking of facts within its possession and taxing stock with a value of $7.00 per share upon an arbitrary value of $33.33 1-3 per share (i. e. five cents per share as compared to fifteen cents per share on stock having a par value of $100, under Section 5503) amounts to a confiscation of appellant's property and to a denial of the equal protection of the law.

5.

The Computation of the Annual Fee Charged Foreign Corporations on the Basis of Their Authorized Stock While Domestic Corporations are Charged on the Basis of Their Subscribed or Issued Stock Results in a Flagrant Discrimination in Favor of Domestic Corporations

The license fee sought to be imposed is not one required as a condition precedent to the corporation's admission into the State, and cases holding that the State

may impose such conditions as it desires have no application. Appellant complied with all the conditions required by the State for its admission to do business therein and became a domesticated foreign corporation in September of 1920. (Record page 2-3.)

At the time of its admission into the state the annual fee required of domestic corporations having stock without par value was computed on the basis of ten cents per share of its subscribed or issued stock. (108 O. L. pt. II. 1287). The annual license fee then prescribed for foreign corporations having stock without par value was one cent per share on its authorized capital stock. The difference in rate tended to compensate the inequality caused by the different basis for the fee.

By the Act of May 17, 1921, the section prescribing the rate for both foreign and domestic corporations having stock without par value was amended so as to require a fee of five cents per share *upon the issued and outstanding stock* of domestic corporations, and five cents per share *upon that proportion of the authorized capital stock* of foreign corporations represented by its property owned and used and business transacted within the state. The effect of the change was to cause foreign corporations having a substantial portion of their authorized capital stock unissued to pay a much larger fee than was required of domestic corporations with the same amount of capital invested and enjoying the same, if not greater privileges. This is well illustrated by the situa-

tion in which the appellant found itself. At the time of its admission into the state in 1920, the fee required was $4,000, provided it transacted all its business in Ohio. The fee computed under the statute as amended in 1921, required the plaintiff to pay an annual fee of $20,000 although only a little more than 50,000 of its 400,000 shares of common stock without par value were then issued and outstanding. A domestic corporation with the same authorized and issued stock as appellant would have been required to pay only $2,524.25, or practically twelve and one-half per cent of the amount assessed against appellant.

Relying upon the ratio for the computation of the annual franchise fee, appellant entered the State and acquired two specially constructed factory buildings, equipped with valuable machinery for the manufacture of electric appliances and representing a total investment of more than $485,000, of which $232,000 was used in the purchase and installation of machinery for the production of electric appliances. The number of corporations engaged in similar enterprises is limited, so that the fixed assets of the company were not readily salable and were not easily convertible, (Record pages 24-25). Their position is therefore distinguishable from that of the White Company in *Cheney Brothers Company v. Massachusetts*, 246 U. S. 147, 156, where the complaining corporation owned a garage and storage building.

It seems to us that the appellant's position is clearly within the doctrine of *Southern Railway Company v. Greene*, 216 U. S. 400, in which the familiar principle announced in *Western Union Telegraph Co. v. Kansas*, 216 U. S. 1, that a corporation which has been admitted to do business within a state cannot be discriminated against unless in accordance with a classification having a real and substantial basis and that the difference of foreign and domestic corporations is not such a basis, was applied.

It is claimed that the doctrine of these cases has been somewhat limited by *Kansas City etc. Ry. Co. v. Stiles*, 242 U. S. 111, and *Cheney Brothers Co. v. Massachusetts* supra. Neither of these cases, however, presents a situation analogous to the one under consideration. In the former, an annual tax imposed by the State of Alabama was computed upon the basis of the paid-up capital stock upon both domestic and foreign corporations. The rate was slightly higher for domestic corporations but the tax was found to be reasonable and in effect at the time the corporation entered the state, and the basis for the tax was the same for both classes of corporations. In the *Cheney* case, a Massachusetts statute imposing an annual tax measured by the authorized capital stock was under consideration. The amount of the tax was small with a maximum of $2,000, which was relied upon to distinguish it from the situation presented in the *International Paper Co. v. Massachusetts* supra, and *Looney v.*

Crane supra. In addition, there was no attempt to discriminate between domestic and foreign corporations.

That cases involving corporation taxes must be determined upon their own peculiar facts has been repeatedly held. *Baltic Mining Co. v. Massachusetts*, 231 U. S. 68; *Kansas City Ry. Co. v. Kansas*, 240 U. S. 227; *Kansas City etc. Ry. v. Stiles*, 242 U. S. 111, 119.

The facts of this case, when considered, disclose a situation which cannot but result in flagrant discrimination. As previously pointed out, requiring foreign corporations to pay a fee computed on the basis of their authorized capital stock, whereas domestic corporations are required to pay on the basis of their issued stock, results in this case in the charging of a fee nearly eight times as great as would be imposed on a domestic corporation, and the appellant has actually been assessed nearly eight times as much as would be assessed against an Ohio corporation with exactly the same authorized and issued capital stock.

Assume that appellant corporation with all of its property located in Ohio, and any one of the many domestic corporations with which it is engaged in severe competition each manufactured and sold in intra and interstate commerce 20,000 washing machines or vacuum cleaners each and that both had identically the same amount of authorized and subscribed, issued and outstanding stock. The tax against appellant is one dollar per machine while its competitor will pay but approximately

sixteen cents per machine. Can such a law be said to give equal protection of the law to citizens of different states? We submit that it not only denies that, but confiscates property without due process of law.

More competition and resulting cheaper prices has been the outcry in this state and nation for the last decade and many have been punished for stifling it. With such laws in the books and spirit in the air it is contrary to all justice and reason for a state to pass a law that not only stifles competition but throttles it. This law forces appellant to add a material figure to the cost of its articles over and above that which its competitor must add. As more than sixty per cent of its product is sold in interstate commerce, we submit even though that statute disclaims any attempt to tax interstate commerce, it in effect does so, placing a severe burden thereon because the basis used is the unfair one, of proportion of the authorized stock, instead of the proportion of the subscribed, issued and outstanding stock.

A tax of $20,000 as compared to appellant's property and business in the state, merely for the privilege of doing business for one year, which, of course, is in addition to the initial fee and property taxes, is further evidence of the unreasonableness of a classification under which such an exorbitant fee can be assessed. The rate at which the fee is computed was greatly increased after the corporation had been admitted to the state, so that it cannot be said to have agreed to such an excessive franchise fee at the time of its entrance in the state.

In this connection, it is instructive to examine the annual franchise fees which are exacted by other states:

Eight states require no annual license fee from either domestic or foreign corporations. They are, District of Columbia, Florida, Louisiana, Minnesota, Mississippi, Nevada, South Dakota and Wyoming. Twenty-four states, Alabama, Arizona, Arkansas, California, Colorado, Connecticut, Georgia, Idaho, Illinois, Iowa, Kentucky, Michigan, Missouri, Montana, Nebraska, New Mexico, New York, North Carolina, Pennsylvania, Tennessee, Utah, Vermont, Washington and Wisconsin, compute the fee required on the same basis for domestic and foreign corporations. Delaware and New Jersey tax on the same basis except that a reciprocal tax is required in the case of foreign corporations. In the remaining states foreign and domestic corporations are taxed on a different basis but owing to the small fee charged with a low maximum the gross inequalities arising under the Ohio law are not possible. The nearest approach to an arbitrary discrimination against foreign corporations is found in Oklahoma, West Virginia and Texas. In the former states the fee charged foreign corporations is 100 per cent and 50 per cent respectively more than required of domestic. In each case the rate is low, however, the inequality is fixed and is of such an amount as might be claimed to be not disproportionate to the different privileges conferred. The Texas statute purports to compute the fee on the same basis as Ohio, i. e., the author-

ized capital stock for foreign corporations and issued for domestic. This statute, however, was construed in *Staples v. Kirby Petroleum Co.*, 250 S. W. 293,(Tex. Civ. App.), to mean actual capital employed and hence subscribed and issued stock. So applied, there is no discrimination.

Under the Ohio law as construed by Ohio courts, *Bedford Coal Co. v. Fulton*, 98 O. S. 350, 354, the par value of the authorized shares is taken without regard to the actual capital employed. The effect is a manifest and frequent discrimination against foreign corporations, bearing without reason or regularity upon foreign corporations and resulting in a tax eight times as great as required of domestic corporations in the present case.

6.

Section 8728-11 As Amended in 109 Ohio Laws, Page 273, Is Unconstitutional As Being Retroactive, Or Action of Appellees Illegal As They Give The Same A Retroactive Effect.

Appellees' answer to the amendment of the bill of complaint filed December 13, 1921 admits that Section 8728-11, as amended in 109 Ohio Laws 273, 277, became effective on the 14th day of August, 1921. Because of the provisions found in Section 5499, appellant was required to and did file a report to the Tax Commission of the State of Ohio during the month of July, 1921, and the report which it did file was based upon Section 5503 of the General Code of the State of Ohio, as shown by

Exhibit No. 2 following page 28 of the record, for no provision was made in said report for any report of stock other than par value stock.

Section 5506 of the General Code of the State of Ohio provides that such fees shall be a first and best lien on all of the property of the corporation, and it has been held such lien attaches as of the date of the filing of the report.

We submit that, the appellees having admitted that said Section 8728-11 was not in effect until August 1, 1921, that none of the defendants could legally fix any such fee as against appellant as would be based upon that particular section, for in doing so appellees clearly place a retroactive effect upon such statute, which is contrary to Section 28, Article 2 of the Constitution of the State of Ohio.

CONCLUSION

For the reasons stated, we submit that the decree of the District Court should be reversed in so far as it upholds the arbitrary basis and classification resulting from the application of Section 8728-11 and Section 5503 of the General Code.

Respectfully submitted,

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